

Breaking the Chains that Bind: Arbitration Agreements Versus Forum Rights Under the Commodity Futures Trading Commission Act of 1974

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Although Congress enacted legislation in 1974 to prohibit predispute arbitration agreements, the Commodity Futures Trading Commission (CFTC) has adopted a regulation allowing predispute arbitration agreements if customers are given the warning prescribed by the Commission. Since the 1974 legislation, some federal courts have refused to defer to the jurisdiction of the CFTC. The regulation adopted by the Commission and the cases refusing to defer to the jurisdiction of the Commission threaten to nullify the intent of Congress that arbitration be voluntary.

INTRODUCTION

With the Commodity Futures Trading Commission Act of 1974¹ (CFTC Act of 1974), the Commodity Exchange Act² underwent its first comprehensive revision since 1936.³ One of the most contro-

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1. Pub. L. No. 93-463, 88 Stat. 1389 (codified at 7 U.S.C. §§ 2-22 (1976)).

2. 7 U.S.C. §§ 1-22 (1976).

3. Federal regulation of commodity futures markets dates from 1922 when Congress enacted the Grain Futures Act, ch. 369, § 1, 42 Stat. 998 (1922) (current version at 7 U.S.C. §§ 2-22 (1976)), to prevent manipulation of commodity futures markets. Wolff, *Comparative Federal Regulation of the Commodities Exchange*

versial innovations of the CFTC Act of 1974 concerns the forum in which brokers and customers can litigate disputes over commodity futures contracts.⁴

One might think that the issue of the forum in which a dispute between a broker and a customer should be decided would be merely a question of different procedures. In fact, winning or losing can depend on the forum in which a dispute is decided.⁵ Thus, the most intensely litigated issues will often revolve around the forum in which the case will be decided.

The traditional forum for broker-customer disputes was arbitration, either before an exchange arbitration panel or before the

and the National Securities Exchanges, 38 GEO. WASH. L. REV. 223 (1969). The Grain Futures Act was amended in 1936 and its name changed to the Commodity Exchange Act—the name of the act under which commodity futures markets are regulated today. Ch. 545, § 1, 49 Stat. 1491 (1936) (codified at 7 U.S.C. §§ 1-22 (1976)).

4. A commodity futures contract is a contract in which there are two parties, a seller and a buyer. The seller promises to deliver a commodity at a future date, hence “futures” contract. The buyer promises to accept delivery of a commodity. *See generally* S. ANGRIST, *SENSIBLE SPECULATING IN COMMODITIES* (1972); H. BAKKEN, *FUTURES TRADING IN LIVESTOCK* (1970); G. GOLD, *MODERN COMMODITY FUTURES TRADING* (1959); B. GOULD, *DOW JONES-IRWIN GUIDE TO COMMODITIES TRADING* (1973); T. HIERONYMUS, *ECONOMICS OF FUTURES TRADING* (1971); C. KELTNER, *HOW TO MAKE MONEY IN COMMODITIES* (1960); S. KROLL & I. SHISKO, *THE COMMODITY FUTURES MARKET GUIDE* (1973); R. TEWELES, C. HARLOW & H. STONE, *THE COMMODITY FUTURES GAME* (1974).

The quantity, quality, and delivery terms of commodity futures contracts are standardized and stated in rules and regulations of the exchanges on which a contract is traded. Delivery dates are at specified monthly intervals.

The performance of commodity futures is secured by money or other property called “margin.” Margin is required to be deposited and maintained at minimum levels prescribed by exchanges. Because commodity futures contracts are standardized and performance is secured, performance does not depend on the finances of the individuals. This imparts a fungibility to commodity futures contracts. Jones & Cook, *The Commodity Futures Trading Commission Act of 1974*, 5 MINN. ST. U.L. REV. 457, 460 (1975).

Price is the only negotiated term in a commodity futures contract. Price must be negotiated by brokers who are members of an exchange on which a contract is traded. Commodity Exchange Act § 4, 7 U.S.C. § 6 (1977 Supp.). Commodity futures contracts must also be executed by open bidding. Commodity Exchange Act § 4b, (D), 7 U.S.C. § 6 (1976). 17 C.F.R. § 1.38 (1978). *See* Julian M. Marks, 20 Agric. Dec. 173 (1961).

This bidding takes place on the floors of exchanges at areas called “pits” or “rings.” Orders are transmitted to floor brokers who bid with other floor brokers for execution of orders. After a customer’s order is executed or “filled,” the broker sends his customer a statement confirming the execution of the order. This confirmation statement will be the only documentation of the execution of a customer’s contract. Because commodity futures contracts are standardized, customers do not execute written contracts.

5. “[A]rbitration, whatever its merit or shortcomings, substantially affects the cause of action created The nature of the tribunal where suits are tried is an important part of the parcel of rights behind a cause of action. The change from a court of law to an arbitration panel may make a radical difference in ultimate result.” *Bernhardt v. Polygraphic Co., Inc.*, 350 U.S. 198, 203 (1956).

American Arbitration Association (AAA). Generally, brokerage firms required customers to agree to arbitrate all future controversies. These arbitration agreements were enforceable under the Federal Arbitration Act, applicable to contracts involving transactions in interstate commerce.⁶ Unless a customer could muster grounds for defeating an arbitration agreement, customers were bound by arbitration agreements to submit all controversies with their brokers to arbitration.⁷

Congress passed the CFTC Act of 1974 to "break the chains" of arbitration agreements. The first innovation concerning forum in the CFTC Act of 1974 is a provision that opened the courtroom door to customers by requiring that arbitration agreements be voluntary.⁸

On November 24, 1975, the Commodity Futures Trading Commission (CFTC) proposed Regulation section 180.3 to implement the mandate of the CFTC Act of 1974 that arbitration be voluntary.⁹ The proposed regulation prohibited brokerage firms from entering into predispute arbitration agreements with customers. The prohibition of predispute arbitration agreements provoked criticism from commodity futures brokers and from the AAA.¹⁰ The CFTC reacted to this criticism by adopting a rule that allows brokers to bind customers to predispute arbitration agreements

6. 9 U.S.C. §§ 1-14 (1976). See M. DOMKE, *THE LAW AND PRACTICE OF COMMERCIAL ARBITRATION* §§ 4.01, .03 (1968). More than one-half of the states have statutes making enforceable arbitration agreements of future disputes. See D. DOBBS, *REMEDIES* 937-38 (1973).

7. See, e.g., *Robinson v. Bache & Co.*, 227 F. Supp. 456 (S.D.N.Y. 1964).

8. The CFTC Act of 1974 provides in § 209 that each commodity futures market shall provide a fair and equitable procedure through arbitration or otherwise for the settlement of customers' claims and grievances against any member or employee thereof: Provided, That (i) the use of such procedure by a customer shall be voluntary, (ii) the procedure shall not be applicable to any claim in excess of \$15,000, (iii) the procedure shall not result in any compulsory payment except as agreed upon between the parties, and (iv) the term "customer" as used in this subsection shall not include a futures commission merchant or a floor broker.

7 U.S.C. § 7a(11) (1976).

9. 40 Fed. Reg. 54,430, 54,435 (1975). Part 180.3(a) stated that [t]he use by customers of the procedure established by a contract market pursuant to the Act shall be voluntary. In that connection the procedure established shall prohibit any agreement or understanding pursuant to which customers agree to submit claims or grievances for settlement under the procedure so established prior to the time when the claim or grievance arose.

10. 41 Fed. Reg. 27,526 (1976).

provided customers are given a bold-faced caveat prescribed by the Commission.¹¹

The second innovation concerning forum in the CFTC Act of 1974 is a provision that opened the CFTC itself as a forum. The Act permits a customer to initiate a proceeding before the CFTC to seek reparation for losses caused by a violation of the Commodity Exchange Act.¹²

In the short time that the CFTC Act of 1974 has been on the books, the courts have decided several cases dealing with the contest over forum. Some courts have shown a reluctance to defer to the jurisdiction of the CFTC. As a consequence, a conflict is developing between the jurisdiction of the courts and that of the CFTC.

This article first outlines arbitration agreements prior to the CFTC Act of 1974. It then considers the implications of section 180.3. Finally, the article analyzes the developing jurisdictional conflict between the courts and the CFTC and suggests a solution to the problem.

11. 17 C.F.R. § 180.3 (1978). The caveat prescribed by the regulation states:

WHILE THE COMMODITY FUTURES TRADING COMMISSION (CFTC) RECOGNIZES THE BENEFITS OF SETTling DISPUTES BY ARBITRATION, IT REQUIRES THAT YOUR CONSENT TO SUCH AN AGREEMENT BE VOLUNTARY. YOU NEED NOT SIGN THIS AGREEMENT TO OPEN AN ACCOUNT WITH [name]. See 17 CFR 180.1-180.6.

BY SIGNING THIS AGREEMENT, YOU MAY BE WAIVING YOUR RIGHT TO SUE IN A COURT OF LAW, BUT YOU ARE NOT WAIVING YOUR RIGHT TO ELECT AT A LATER DATE TO PROCEED PURSUANT TO SECTION 14 OF THE COMMODITY EXCHANGE ACT TO SEEK DAMAGES SUSTAINED AS A RESULT OF A VIOLATION OF THE ACT. IN THE EVENT A DISPUTE ARISES, YOU WILL BE NOTIFIED IF [name] INTENDS TO SUBMIT THE DISPUTE TO ARBITRATION. IF YOU BELIEVE A VIOLATION OF THE COMMODITY EXCHANGE ACT IS INVOLVED AND IF YOU PREFER TO REQUEST A SECTION 14 'REPARATIONS' PROCEEDING BEFORE THE CFTC, YOU WILL STILL HAVE 45 DAYS IN WHICH TO MAKE THAT ELECTION.

An agreement which does not comply with this form is ineffective. *Wanty v. Sprow* [Current Binder] COMM. FUT. L. REP. (CCH) ¶ 20,548 (S.D.N.Y. 1978).

12. 7 U.S.C. § 18 (a)-(i) (1976). Subsection (a) provides:

Any person complaining of any violation of any provision of this chapter or any rule, regulation, or order thereunder by any person registered under section 6d, 6e, 6j, or 6m of this title may, at any time within two years after the cause of action accrues, apply to the Commission by petition, which shall briefly state the facts, whereupon, if, in the opinion of the Commission, the facts therein contained warrant such action, a copy of the complaint thus made shall be forwarded by the Commission to the respondent, who shall be called upon to satisfy the complaint, or to answer it in writing, within a reasonable time to be prescribed by the Commission.

ARBITRATION AGREEMENTS BEFORE THE CFTC ACT OF 1974

Exchange Arbitration

The Arbitration Panel

Before the CFTC Act of 1974, the first and decisive issue in customer-broker controversies was whether a customer could be compelled to arbitrate his dispute with a broker. Arbitration agreements were ensconced in form contracts that could run to as many as twenty paragraphs of fine print. Typically, a customer agreed to submit all future controversies which might arise between the customer and the brokerage firm to arbitration. Arbitration agreements permitted election by the customer of arbitration either by the procedure of the exchange on which the transaction was executed, by the procedure of the New York Stock Exchange (NYSE), or by the procedure of the AAA. If the customer did not elect within five days after his brokerage firm requested him to do so, the brokerage firm could elect the procedure to be followed.¹³

These arbitration agreements appeared innocuous but were a pitfall for customers. Customers seldom struggled through the fine print of the form contracts they were given to sign when they opened an account. Even if a customer read the arbitration agreement in his contract, he probably did not know what he had to do to protect his rights. If, as a consequence of not knowing what to do, a customer did nothing, he could lose any claim he had.

Although customers often failed to act, brokerage firms did not fail to act. Brokerage firms elected arbitration by an exchange procedure because the arbitrators were brokers. However, the ar-

13. An example of such an agreement provides that:

Any controversy between you and the undersigned arising out of or relating to this contract or the breach thereof, shall be settled by arbitration in accordance with the rules, then obtaining, of either the American Arbitration Association, or the Board of Arbitration of the New York Stock Exchange, or any other organized market or Board of Trade or exchange of which you are a member and upon which the transaction was executed, as the undersigned may elect. If the undersigned does not make such election by registered mail addressed to you at your main office within five (5) days after receipt of notification from you requesting such election, then the undersigned authorizes you to make such election in behalf of the undersigned. Any arbitration hereunder shall be before at least three arbitrators and the award of the arbitrators, or of a majority of them, shall be final, and judgment upon the award rendered may be entered in any court, state or federal, having jurisdiction.

M. DOMKE, *supra* note 6, § 5.04.

bitration agreements did not state that under exchange arbitration procedure the arbitrators would be brokers.

Commodity exchange arbitration occurred before a committee of exchange members. Customers had no choice of arbitrators.¹⁴ The arbitration procedure of the NYSE allowed customers to elect to have three of the five arbitrators appointed from a panel of persons who were not brokers.¹⁵ The Board of Directors of the NYSE appointed this panel;¹⁶ the customer had no say in who was chosen. Thus, arbitration panels of brokers, or of brokers and persons appointed by brokers, decided claims of customers against brokers.

Many persons who sat on exchange arbitration panels undoubtedly tried to be impartial. However, one would be naive to believe that brokers were not biased in favor of their fellow brokers. For those in the same business or profession to empathize with one of their own in a conflict with an outsider is human nature.¹⁷ Nevertheless, a customer could not avoid arbitration on the ground of bias.¹⁸

Because arbitration agreements did not state that exchange arbitration would be before brokers, most customers probably assumed that the arbitration panel would be impartially composed. By the time they realized that it would not be, it was too late to do anything about it. A customer caught by an agreement that compelled him to submit his claim to arbitration before an exchange found himself in a predicament. Instead of litigating his claim before his peers in his own community, he faced a trip to Chicago or to New York to submit his claim to a panel of brokers. If a customer was poor, or if his claim was small, the expense of travel and lodging for him, for his attorney, and for an expert witness could be enough to deter his claim.¹⁹

14. *E.g.*, Rule 180 of the Chicago Board of Trade; Rule 501 of the Chicago Mercantile Exchange; Sec. 6.03 of the Rules of the New York Cotton Exchange.

15. [1979] NEW YORK STOCK EXCHANGE, INC., CONSTITUTION AND RULES (CCH) ¶ 2484, at 4127 (Rule 484 of the Board of Directors).

16. *Id.* ¶ 1354, at 1071-2 to 1071-3, ¶ 1356, at 1071-3 to 1072 (NYSE Const., art. VIII, §§ 4, 6).

17. *See* PROFESSIONAL NEGLIGENCE 5 (T. Roady & W. Anderson eds. 1960).

18. *See, e.g.*, *Tamari v. Bache & Co.*, 565 F.2d 1194, 1202 (7th Cir. 1977); *Arrieta v. Paine, Webber, Jackson & Curtis, Inc.*, 59 Cal. App. 3d 322, 329-30, 130 Cal. Rptr. 534, 538 (1976); *Feldman, Arbitration Law in California: Private Tribunals for Private Government*, 30 S. CAL. L. REV. 375, 449 (1957).

19. One person familiar with exchange arbitration has observed that customers are deterred from arbitration by the inability to pay the filing fee prescribed by an exchange. *New York Chamber of Commerce, The Disputed Transaction: How Arbitration Is Used in the Securities Industry* 8 (1967) (statement of H. Vernon Lee).

No Discovery in Arbitration

Arbitration agreements were part of form contracts prepared by brokerage firms. These form contracts never provided for discovery.²⁰ Unless an arbitration agreement provides for discovery, generally no right to discovery on the merits exists.²¹ Likewise, the arbitration rules of exchanges did not provide for discovery.²² One attorney described arbitration as "a throw back to the system of surprise at trial."²³

Customers often needed discovery to prove their claims. For example, a customer seeking to prove that a broker caused his account to be traded excessively ("churned") would need evidence of the amount of trading of other accounts to compare with his account.²⁴ Similarly, a customer might need evidence from a brokerage firm employee beyond the reach of subpoena. Without the aid of discovery, the customer was limited to proving a case on the basis of evidence he already had.

The General Submission Agreement

Arbitrators derive their authority from the agreement referring a dispute to arbitration, called a "submission agreement."²⁵ The aspect of exchange arbitration that provoked the most criticism was the absolute authority arbitrators had under submission agreements.²⁶ A general submission agreement defines neither the issues to be decided nor the way the issues are to be decided, but gives arbitrators plenary power in deciding all rights in dispute.²⁷

20. See NEW YORK INSTITUTE OF FINANCE, A PRIMER ON BROKERAGE OPERATIONS 16 (1973) for the standard form of agreement.

21. See *Mississippi Power Co. v. Peabody Coal Co.*, 69 F.R.D. 558, 566 (S.D. Miss. 1976); M. DOMKE, *supra* note 6, at 265, 271.

22. *E.g.*, Rules 180-99 of Chicago Board of Trade; Rules 500-09 of the Chicago Mercantile Exchange; Secs. 6.01-.03 of Rules of New York Cotton Exchange.

23. New York Chamber of Commerce, *The Disputed Transaction: How Arbitration Is Used in the Securities Industry* 46-47 (1967) (statement of Robert Lunney).

24. See, *e.g.*, *Booth v. Peavey Co. Commodity Servs.*, 430 F.2d 132 (8th Cir. 1970).

25. See M. DOMKE, *supra* note 6, at 99; J. REDMAN, *LAW OF ARBITRATIONS AND AWARDS* 1 (4th ed. 1903).

26. See, *e.g.*, E. BRODSKY, *GUIDE TO SECURITIES LITIGATION* 303 (1974); Comment, *Arbitration of Investor-Broker Disputes*, 65 CALIF. L. REV. 120, 129 (1977).

27. See *Marchant v. Mead-Morrison Mfg. Co.*, 252 N.Y. 284, 169 N.E. 386, *aff'd*, 226 App. Div. 397, 235 N.Y.S. 370 (1929); J. MORSE, *LAW OF ARBITRATION AND AWARD* 5 (1902); J. REDMAN, *LAW OF ARBITRATIONS AND AWARDS* 79 (4th ed. 1903).

Arbitrators deciding a controversy submitted on a general submission have virtually unlimited discretion.²⁸ Consequently, they are not bound to decide a controversy in conformity with law but may decide it on broad principles of justice and equity.²⁹ Furthermore, an award decided under a general submission cannot be attacked on the basis of errors on the law or on the facts.³⁰ Even if it were possible to set aside an arbitration award tainted with error, a general submission makes it virtually impossible to show such an error³¹ because arbitrators deciding a controversy on a general submission are not required to state reasons for their decision.³²

Most agreements to submit future controversies to arbitration are general submission agreements.³³ Consider, then, what a customer in a dispute faced. A customer who had been caught up in exchange arbitration faced the prospect of having his claim against a broker being decided by brokers. If arbitration was before a NYSE panel, his claim would be decided by brokers or a mixed panel of brokers and persons appointed by brokers if a customer was alert enough to choose to have nonbrokers on his panel. Arbitrators did not have to decide according to the law. They had no duty to state reasons for a decision, and errors of law or fact could not be reviewed.

How did customers fare in exchange arbitration? How did the

28. In *Muldow v. Norris*, 2 Cal. 74, 77 (1872), the court rather elegantly stated: [U]nder a general submission, arbitrators have power to decide upon the law and facts: and a mere mistake of law cannot be taken advantage of. The arbitrators are not bound to award, on principles of dry law, but may decide on principles of equity and good conscience, and make their award *ex aequo et bono*.

29. See, e.g., *Sapp v. Barenfeld*, 34 Cal. 2d 515, 523, 212 P.2d 233, 239 (1949); *Crofoot v. Blair Holdings Corp.*, 119 Cal. App. 2d 156, 186, 260 P.2d 156, 172 (1953); *Everett v. Brown*, 120 Misc. 349, 198 N.Y.S. 462 (1923).

30. In *Wilkins v. Allen*, 169 N.Y. 494, 496-97, 62 N.E. 575, 576 (1902), the court stated that:

The award of an arbitrator cannot be set aside for mere errors of judgment either as to the law or as to the facts. If he keeps within his jurisdiction, and is not guilty of fraud, corruption, or other misconduct affecting his award, it is unassailable, operates as a final and conclusive judgment, and . . . the parties must abide by it.

See also *Wilko v. Swan*, 346 U.S. 427, 436 (1953); *Orion Shipping and Trading Co. v. Eastern States Petroleum Corp.*, 312 F.2d 299, 300 (2d Cir. 1963); *Jones v. Kvistad*, 19 Cal. App. 3d 836, 97 Cal. Rptr. 100 (1971); *Underhill v. Van Cortlandt*, 2 Johns. Ch. 340 (N.Y. 1817).

31. See M. DOMKE, *supra* note 6, at 260; Comment, *Arbitration of Investor-Broker Disputes*, 65 CALIF. L. REV. 120, 129 (1977).

32. See *Case v. Alperson*, 181 Cal. App. 2d 757, 761, 5 Cal. Rptr. 635, 638 (1960) ("It is not incumbent on the arbitrators to make findings of fact, to give reasons back of their award, nor to tell how it was reached"); W. STURGES, *COMMERCIAL ARBITRATION AND AWARDS* 533-34 (1930).

33. See M. DOMKE, *supra* note 6, at 44, 47. See, e.g., [1979] NEW YORK STOCK EXCHANGE, INC., CONSTITUTION AND RULES (CCH) ¶ 2492A, at 4129-4131.

Christians fare with the lions? No one can demonstrate how customers fared because no written decisions exist. Considering the affinity brokerage firms had for exchange arbitration, however, one might suspect that customers did not fare well.³⁴ However, once in a while one caught a glimpse of what happened behind closed doors. One such glimpse came from the notorious case of *Sobel v. Hertz, Warner & Co.*³⁵ The customer submitted to a NYSE arbitration panel a dispute involving, among other issues, charges against his broker of market manipulation, secret payoffs to securities salesmen in return for stock recommendations, and the creation of false markets. The arbitrators dismissed the customer's claim. They stated no reason for their decision—the general submission agreement required none. After the dismissal, the customer's broker entered a guilty plea to criminal charges involving the same misconduct upon which the customer had based his arbitration claim.

The customer sought to have the arbitrators state the reasons for their decision, no doubt as a preliminary step to attacking the decision. Despite the broker's admitted plea of guilty, the customer was unable to compel the arbitrators to state a basis for their decision. Because the arbitration had been decided on a general submission, the court of appeals held that the arbitrators did not have to state reasons for their decision.

American Arbitration Association Proceedings

AAA Geared Against Deciding Cases on the Basis of Law

Although AAA arbitration is an institution often defended with a zealousness approaching the defense of motherhood and the flag, AAA arbitration was actually as deadly for a customer's case as an exchange arbitration. The pitfall to a customer of arbitrating a claim before the AAA may have been more subtle than the pitfall of exchange arbitration. Bias against the customer was inherent in AAA arbitration proceedings rather than in the arbitrators themselves.

For many commercial disputes, AAA arbitration is a good method of resolving controversies. The strengths of AAA arbitration are its informality and its use of impartial arbitrators who

34. See Comment, *Arbitration of Investor-Broker Disputes*, 65 CALIF. L. REV. 120, 130 (1977).

35. 469 F.2d 1211 (2d Cir. 1972).

have expertise in the matter in dispute. In the words of Judge Learned Hand, "one of the chief advantages of arbitration is that arbitrators can be chosen who are familiar with the practices and customs of the calling, and with just such matters as what are current prices, what is merchantable quality, and what are the terms of sale, and the like."³⁶ For commercial disputes of the kind described by Judge Hand, arbitration is better than litigation because

[t]he very refinements and complexities of our court machinery often make it cumbersome and dilatory when applied to controversies involving simple issues of fact or law. This is especially true in the case when the issue of fact turns upon expert knowledge as to the nature or quality of merchandise or the damage consequent upon the failure to perform a contract for its delivery . . . which can be better determined by a layman having training and experience in a particular trade or business than by a judge and jury who have not had that training and experience.³⁷

But the virtues of arbitration in deciding many commercial disputes are vices in deciding controversies involving more than the most rudimentary concepts of law. As with arbitration generally, AAA arbitrators are not instructed on the law.³⁸ This lack of instruction is consistent with the view that the law should play a minor part in arbitration.³⁹ In speaking of the difference between arbitration and litigation one commentator observed that

[i]t isn't "just like the courts." In fact, its strongest points lie in those areas where it most widely differs from the courts. Arbitration and litigation have a similar goal. The proceedings of the two processes are somewhat alike, principally because the arbitration proceeding has been altered to accommodate the lawyer. In both processes questions of fact pertaining to the dispute at hand are critical. The major difference is the framework within which these questions are examined. The rules of law which provide such a framework in litigation are at most a minor part of the arbitration process.⁴⁰

But even more important than the minor role of the law in arbitration generally (and then in deference to lawyers) is that AAA arbitration is actually geared against deciding disputes on the basis of law.

36. *American Almond Products Co. v. Consolidated Pecan Sales Co.*, 144 F.2d 448, 450 (2d Cir. 1944).

37. 10 PROCEEDINGS OF THE ACADEMY OF POLITICAL SCIENCE 197 (1923) (statement of Chief Justice Harlan F. Stone), reprinted in M. DOMKE, *supra* note 6, at 11.

38. See *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 407 (1967) (Black, J., dissenting); M. DOMKE, *supra* note 6, at § 25.06.

39. The court in *Everett v. Brown* stated that arbitrators are usually laymen, inexperienced in the technical rules of law, but usually possessed with a fund of common sense which enables them to do substantial justice between the parties. To require an arbitrator to follow the fixed rules of law in arriving at his award would operate to the defeat of the object of the proceeding.

120 Misc. 349, 351, 198 N.Y.S. 462, 465 (1923).

40. AMERICAN MANAGEMENT ASS'N, RESOLVING BUSINESS DISPUTES 102 (1965), quoted in M. DOMKE, *supra* note 6, at § 1.01.

Unless a lawyer happens to be on a panel, arbitrators will have no legal background. Because AAA arbitrators are given no instructions of law, obviously AAA arbitration must be geared against deciding questions of law. Indeed, AAA arbitrators are cautioned not to state reasons for their decision so as to discourage any judicial review.⁴¹ AAA arbitrators are unpaid volunteers. A practical reason for AAA arbitrations being decided on a general submission is that unpaid volunteers are not expected to take the time or make the effort to state reasons for decisions.⁴² AAA arbitrators thus eschew reasoning their decisions in writing, an intellectual discipline required of judges.

AAA arbitration is stacked against a customer because his case is typically built on legal principles. A customer's case is a lawyer's case. Typically, customers contend that a broker has violated the Commodity Exchange Act or a rule or regulation promulgated under the Act.⁴³ The Commodity Exchange Act and the rules promulgated under the Act are basically specialized applications of the common law to the milieu of commodity futures trading. The duties of a brokerage firm to a customer are analogues to common law rules of agency, pledges, and deceit.⁴⁴

In his education, a lawyer must spend only a few hundred hours reading the law of agency, deceit, and pledges to grasp the law involved in the typical dispute between a broker and a cus-

41. M. DOMKE, *supra* note 6, at § 29.05.

42. See New York Chamber of Commerce, *The Disputed Transaction: How Arbitration Is Used in the Securities Industry* 18 (1967) (statement of Robert Coulson, Executive Vice-President, American Arbitration Association).

43. See, e.g., *Lincoln Commodity Servs. v. Meade*, 558 F.2d 469 (8th Cir. 1977) (action based on antifraud rule of 7 U.S.C. § 6(b)); *Booth v. Peavey Co. Commodity Servs.*, 430 F.2d 132 (8th Cir. 1970); *Scott v. Lincolnwood, Inc.*, [Current Binder] COMM. FUT. L. REP. (CCH) ¶ 20,447 (CFTC 1977) (action based on violation of Rule 1.33a requiring monthly statement to be sent to each customer who has interest in pooled account); Note, *Private Rights of Action for Commodity Futures Investors*, 55 B.U.L. REV. 804-26 (1975).

44. See C. MEYER, *THE LAW OF STOCKBROKERS AND STOCK EXCHANGES* 7 (1931). The purpose of the antifraud rules provisions in § 4b of the Act, for example, was to incorporate into the Act the agency duties which a broker has toward his customer. See J. BAER & O. SAXON, *COMMODITY EXCHANGES AND FUTURES TRADING* 261 (1949) (setting forth digest written in 1936 by N.M. Mehl, Administrator of the Commodity Exchange Authority, the agency which regulated commodity futures markets before the 1974 Act). Furthermore, one cannot really understand the general antifraud provisions of § 4a, for example, without understanding that a broker has a common law duty to affirmatively disclose to his customer material facts concerning a transaction. *Cecka v. Beckman & Co.*, 28 Cal. App. 3d 5, 11, 104 Cal. Rptr. 374, 377 (1972).

tomer. An unpaid volunteer, unschooled and uninstructed in the law, can hardly grasp the law from a few hours at an arbitration hearing. The absurdity of law decided by those ignorant of the law is glossed over by the general submission agreement. The proponents of arbitration thus know that arbitration would end if arbitrators were required to state reasons for their decisions.⁴⁵

In *Wilko v. Swan*,⁴⁶ the United States Supreme Court held that arbitration agreements that bound customers to arbitrate future disputes with stockbrokers were invalid as being repugnant to the rights a customer has under the Securities Act of 1933. The Court spoke of the inadequacy of arbitration for deciding legal questions:

Even though the provisions of the Securities Act, advantageous to the buyer, apply, their effectiveness in application is lessened in arbitration compared to judicial proceedings. Determination of the quality of a commodity or the amount due under a contract is not the type of issue involved. This case requires subjective findings on the purpose and knowledge of the alleged violator of the Act. They must be not only determined but applied by the arbitrators without judicial instructions on the law.⁴⁷

The same can be said of the rights of a customer under the Commodity Exchange Act.

The Businessman Arbitrator

Not only is the AAA arbitration proceeding geared against deciding cases on the basis of law, the chances are that the concepts of law that the customer must urge will evoke frowns from his listeners. Most AAA arbitrators are businessmen, accountants, business lawyers, bankers, or others interested in business and finance. Most commercial disputes are between two businessmen, but a commodity futures dispute involves a customer versus a businessman.

A broker has a fiduciary duty to his customer,⁴⁸ a duty higher than the "morals of the market place."⁴⁹ The idea of a business-

45. In *Sobel v. Hertz, Warner & Co.*, 469 F.2d 1211, 1215 n.7 (2d Cir. 1972), the New York Stock Exchange filed an amicus brief contending that written decisions would mean the end of securities industry arbitration of customer claims.

46. 346 U.S. 427 (1953).

47. *Id.* at 435-36. The Court noted that the United States Arbitration Act contained no provision for judicial determination of legal issues as was found in English law. *Id.* at 437.

48. See, e.g., *In re Rosenbaum Grain Corp.*, 103 F.2d 656, 661 (7th Cir. 1939). The court stated: "We find that a spirit of trust and fidelity necessarily pervades the entire dealing between broker and customer. This fiduciary relation plus the nature of the dealing itself, affected as it is by the public interest, has led in each instance to parallel regulation by the exchanges, legislatures, and Congress."

49. As Judge Cardozo said: "Many forms of conduct permissible in a workaday world for those acting at arm's length are forbidden to those bound by fiduciary

man having a fiduciary duty to his customer does not square with the *laissez faire* individualism redolent of the 1850s which is the credo of the American businessman. A customer's case smacks of consumerism. A businessman may view the Commodity Exchange Act and rules and regulations of commodity futures trading as further instances of governmental interference with private enterprise.

AAA Arbitration Ideal for Brokers

AAA arbitration is stacked against a customer for the same reason it is stacked in favor of the brokerage firm. AAA arbitration is ideal for a simplistic, that is, nonlegalistic, view of a dispute. If the brokerage firm seeks to collect from a customer, it will present its case as a simple debt collection—the customer promised to reimburse a brokerage firm for money advanced by the brokerage firm and then reneged on his promise. However, if a customer seeks to recover from a brokerage firm, the AAA arbitrator will be impressed that commodity futures trading is risky and that the customer knew or should have known that it was risky. This simplistic view of the facts will impress the arbitrator who will want to get down to “the facts” and will not want to be bothered with a lot of legalistic folderol.⁵⁰

THE CFTC'S VERSION OF VOLUNTARY ARBITRATION AGREEMENTS

The CFTC's Initial Proposal

To inveigle, with a fine-print form contract, a customer into submitting his controversy with a broker to arbitration before a panel of brokers struck some people as unfair to customers.⁵¹ Those who drafted the 1974 amendments to the Commodity Exchange Act recognized this unfairness. In 1973, Alex Caldwell, the Administrator of the Commodity Exchange Authority, stated that

ties. A trustee is held to something stricter than the morals of the market place.” *Meinhard v. Salmon*, 249 N.Y. 458, 464, 164 N.E. 545, 546 (1928).

50. The antagonism of merchants to lawyers and to law courts is a tradition which goes back to Colonial times. M. HORWITZ, *THE TRANSFORMATION OF AMERICAN LAW, 1790-1880*, at 144-49 (1977). One merchant complained that “a Number of Pettifoggers are always ready to . . . puzzell the Laws, which are far from being explicit with respect to Commerce.” *LETTER BOOK OF JOHN WATTS* 337 (Collections of the N.Y. Hist. Soc. for 1928), reprinted in *id.* at 147.

51. *Richards v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 64 Cal. App. 3d 899, 903, 135 Cal. Rptr. 26, 28 (1976).

the practice of compelling customers to submit disputes to arbitration was unfair and that the legislation which the Authority was backing would prohibit predispute arbitration agreements.⁵²

Under the influence of *Wilko v. Swan*,⁵³ predispute arbitration agreements were generally thought to be the antithesis of voluntary arbitration.⁵⁴ The purpose of section 5a of the CFTC Act of 1974 was to adopt the *Wilko v. Swan* prohibition against predispute arbitration agreements. This purpose was seen in the prohibition of predispute arbitration agreements in section 180.3 as originally proposed.⁵⁵ The proposed regulation clearly expressed Congress' intent, but the prohibition of predispute agreements sorely distressed brokers and the AAA. The outcry raised by brokerage firms and the AAA persuaded the CFTC that customers should be bound by predispute arbitration agreements.

Voluntary Means What CFTC Chooses It to Mean

To leap from arbitration agreements that Congress intended to be "voluntary" to agreements that should bind customers, the CFTC rationalized that customers' agreements to predispute arbitration could be deemed "voluntary" if the customers were advised. To make customers' predispute agreements voluntary, section 180.3 requires that customers be advised in bold-face type that they do not have to agree to arbitration and that they could be waiving the right to bring an action in court. A customer's right to choose not to arbitrate is backed up by a decree⁵⁶ against making customers sign an arbitration agreement as a condition for opening an account.

The assumption implicit in the section 180.3 caveat is that customers will read and understand the statement and thus will be able to make a choice free of mistake, fraud, or undue influence. This assumption is a fiction. Customers do not read and study documents they are handed to sign when they open an account.⁵⁷ Customers glance over the three or four documents they are handed and sign them.

The typical customer's agreement is one-sided—the customer

52. Discussion with Alex Caldwell (Oct. 1973). It is generally assumed that the reparations procedure was adopted to avoid the bias of exchange arbitration of customer disputes. See, e.g., Rainbolt, *Regulating the Grain Gambler and His Successors*, 6 HOFSTRA L. REV. 1, 19 (1977).

53. 346 U.S. 427 (1953).

54. *Tamari v. Bache & Co.*, 565 F.2d 1194, 1205-06 (7th Cir. 1977) (Swygert, J., dissenting).

55. 40 Fed. Reg. 54,435 (1975).

56. 17 C.F.R. § 180.3(b)(1) (1978).

57. See, e.g., *Vernon v. Drexel Burnham & Co.*, 52 Cal. App. 3d 706, 714, 125 Cal. Rptr. 147, 151 (1975).

makes all the promises, and the brokerage firm makes no promises. Customers give up all their rights and receive nothing in return from brokerage firms. As one court stated: "[Such an agreement] is totally one-sided for the benefit of the broker. It lacks consideration, because for this entire parting with his rights the customer secures no correlative advantage."⁵⁸

Today's typical customer's agreement⁵⁹ was set forth in a treatise published in 1931.⁶⁰ If customers have been signing such customers' contracts for over forty years, one doubts that customers will suddenly be sufficiently impressed by the section 180.3 caveat to consult a lawyer; and without legal counsel, the average customer will not be able to make an intelligent choice whether to arbitrate. To assume that customers will be able to decide intelligently whether to choose arbitration by reading the section 180.3 statement is as much a fiction as the presumption that everyone knows the law. The average customer knows only vaguely what is involved in the legalese of the caveat. But given the desire of courts to relieve their crowded calendars, the fiction implicit in section 180.3 will not make much difference.⁶¹

For a customer to be adequately warned, he should be advised in language he can easily understand of what he gives up by choosing arbitration. In response to this suggestion, the CFTC stated that: "While the Commission is of the view that the legal implications of the proposed language could be spelled out in all their ramifications, it would be virtually impossible to do so in less than several highly technical paragraphs. The result would be a longer and perhaps more confusing document."⁶² That it

58. *Jones v. De Ronde*, 142 Misc. 831, 835, 255 N.Y.S. 505, 509 (1932).

59. See NEW YORK INSTITUTE OF FINANCE, A PRIMER ON BROKERAGE OPERATIONS 16 (1973).

60. See C. MEYER, THE LAW OF STOCKBROKERS AND STOCK EXCHANGES 747 (1931).

61. See, e.g., *Vernon v. Drexel Burnham & Co.*, 52 Cal. App. 3d 706, 715, 125 Cal. Rptr. 147, 152 (1975).

62. 41 Fed. Reg. 42,944 (1976).

The observation of Commons is appropriate:

There is naturally always a resistance, on the part of those who make the authoritative decisions, against any movement requiring these working rules to be formulated in words and published for the information of all. It is usually contended by them that the rules are so difficult and complex that they can be understood only by experts or those who by long training have become experienced in interpreting them. It was only after a vigorous struggle that the Twelve Tables of the Roman law were published. The Egyptian priests are said to have formulated a principle of the econ-

would be too difficult to tell a customer what he should know to be able to make an intelligent decision demonstrates the falsity of the assumption that by reading the section 180.3 caveat a customer's choice will become voluntary. The difficulty of advising customers of the implications of arbitration, however, was not the reason the CFTC rejected this proposal.⁶³ The CFTC wanted to encourage customers to sign arbitration agreements. To explain to customers the implications of arbitration agreements would not have encouraged arbitration.

The Effect of the Section 180.3 Caveat

Ironically, the customer now has less choice than he did before the CFTC undertook to give the customer a voluntary choice. In the days of the fine-print arbitration agreements, customers had a sporting chance of avoiding arbitration agreements by proving grounds for rescission, usually fraud.⁶⁴ Under section 180.3, the day of the small-print arbitration agreement is no more. The section 180.3 caveat must be stated in large, bold-face print. Furthermore, customers are required to sign a statement that they have read the caveat and that they either agree or do not agree to arbitration. The bold-face caveat of section 180.3 will make it difficult for customers to show grounds for rescission.

The CFTC Act of 1974 also takes away the sanctuary of the federal securities laws. If the controversy arose out of a transaction in a discretionary account, the account could be considered a "se-

omy of the truth in order to justify their refusal to give out the working rules which they were privileged to interpret. And much the same doctrine is formulated by businessmen, bankers, financiers, politicians, labor leaders and others who dread the bad use that might be made of the flexible working rules which they administer, or who flatly deny that the rules are anybody's 'business' but their own.

J. COMMONS, *LEGAL FOUNDATIONS OF CAPITALISM* 141 (1957).

63. The pervasiveness of legalistic governmental regulations is probably due to the unwillingness of lawyers to try to write regulations which can be understood by nonlawyers. See M. BERNSTEIN, *REGULATING BUSINESS BY INDEPENDENT COMMISSIONS* 227 (1966).

64. See *Main v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 67 Cal. App. 3d 19, 136 Cal. Rptr. 378 (1977) (arbitration clause in lending agreement permitting Merrill Lynch to make discretionary sales and purchases for customer's account); W. STURGES, *COMMERCIAL ARBITRATION AND AWARDS* 217 (1930). The fine-print contracts customers were generally required to sign when they opened accounts were contracts of adhesion. *Richards v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 64 Cal. App. 3d 899, 135 Cal. Rptr. 26 (1976). As contracts of adhesion, arbitration agreements were vulnerable to being attacked as having been fraudulently induced. On contracts of adhesion, see *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 407 (1967) (Black, J., dissenting); *Standard Oil Co. v. Perkins*, 347 F.2d 379, 383 (9th Cir. 1965); Kessler, *Contracts of Adhesion—Some Thoughts About Freedom of Contract*, 43 COLUM. L. REV. 629 (1943). But cf. *Berman v. Dean Witter & Co.*, 44 Cal. App. 3d 999, 1003, 119 Cal. Rptr. 130, 132 (1975) (arbitration compelled when customer did not show arbitration agreement was a contract of adhesion).

curity" under the federal securities laws.⁶⁵ Because predispute arbitration agreements were contrary to rights of customers under the federal securities laws, customers could avoid arbitration by alleging a discretionary account. However, commodity accounts are now under the exclusive jurisdiction of the CFTC;⁶⁶ the customer can no longer avoid arbitration under the federal securities laws.

If one equates voluntariness with "informed" choice, the customer now has less opportunity to make a voluntary choice whether to arbitrate than before section 180.3. The customer will not know what is involved in choosing arbitration. He will not have the incentive to seek competent legal advice. Customers do have incentive to seek competent legal advice after a controversy has arisen, but by then a customer probably will already have bound himself to arbitration.

ARBITRATION VS. REPARATION

Although customers now probably have less real choice about whether to arbitrate than before section 180.3, the saving grace for customers is reparation. The CFTC Act of 1974 provides for a reparations procedure by which a customer can obtain compensation for a broker's violation of the Commodity Exchange Act or any rule, regulation, or order thereunder.⁶⁷ Section 180.3 preserves a customer's right to bring a reparations proceeding by allowing him to bring the proceeding within forty-five days after notification by a brokerage firm that it intends to seek arbitration.

One could expect brokerage firms to use arbitration clauses as a way of avoiding reparations proceedings. Brokerage firms are wary of the reparations procedure. Reparations are formal. Decisions are written and published. The reparations procedure is geared toward giving customers redress for violations of the Commodity Exchange Act and rules adopted thereunder. Violations of the Act and the rules are not to be taken lightly in reparations proceedings.

The attitude of the brokerage firms was manifested at a CFTC hearing on arbitration clauses. At the hearing, an attorney for

65. See, e.g., *SEC v. Continental Commodities Corp.*, 497 F.2d 516 (5th Cir. 1974).

66. 7 U.S.C. § 2 (1976).

67. *Id.* § 14.

Merrill Lynch, Pierce, Fenner & Smith, Inc., allowed that although a broker had an obligation to inform the customer of the volatile nature of commodity futures markets, a broker probably did not have a duty to inform a customer that he was "waiving reparation or court rights by signing a pre-dispute arbitration agreement."⁶⁸

The skirmishing for forum began with the very first reparations proceeding, *Hornblower & Weeks-Hemphill Noyes, Inc. v. Csaky*.⁶⁹ A customer who opened an account with \$25,000 brought a reparations proceeding. He contended that the brokerage firm's employee had traded the account and caused losses of \$56,000 in the account. The customer refused to pay the \$31,000 deficit in his account, claiming the brokerage firm had mishandled his account.

The brokerage firm filed an arbitration proceeding with the AAA. On the day before the arbitration hearing, the customer filed a reparation petition with the CFTC. The customer did not appear at the arbitration hearing. The arbitrator awarded \$31,000 to the brokerage firm.

The brokerage firm obtained a judgment on the arbitration award in a state court in New York. The brokerage firm then filed a petition in the United States district court to stay the reparations proceeding which was then pending before the CFTC. However, District Court Judge Stewart denied the brokerage firm's petition. He assumed that because the amount in controversy exceeded \$15,000, the controversy was not subject to arbitration. This assumption was based on the exemption from exchange arbitration of any claim in excess of \$15,000.⁷⁰ However, the court did not on that ground deny the petition because the court considered this question one that should be decided in the first instance by the CFTC. Instead, the court based its decision on the lack of any provision in the Federal Arbitration Act⁷¹ to stay administrative proceedings. "The lack of such a provision is consistent with a long-standing policy of hesitancy to interfere with administrative proceedings before all administrative remedies have been exhausted."⁷²

Deference to the jurisdiction of the CFTC was evident in other cases in which brokers sought to compel arbitration. In *Bache Halsey Stuart, Inc. v. French*,⁷³ Judge Sirica of the United States

68. [1976] 18 COMM. FUT. L. REP. (CCH) 7.

69. [1975-77 Transfer Binder] COMM. FUT. L. REP. (CCH) ¶ 20,270 (S.D.N.Y. 1977).

70. 7 U.S.C. § 5a(11) (1976).

71. 9 U.S.C. §§ 1-14 (1976).

72. [1975-77 Transfer Binder] COMM. FUT. L. REP. (CCH) ¶ 21,471 (citations omitted).

73. *Id.* ¶ 20,249 (D.D.C. 1977).

District Court for the District of Columbia refused to order a customer to proceed with arbitration and refused to enjoin the customer from proceeding with a reparations proceeding. Judge Sirica based his decision on the ground that ordering arbitration would be inconsistent with the underlying purpose of the Commodity Exchange Act. In *Milani v. ContiCommodity Services, Inc.*,⁷⁴ Judge Weigel of the United States District Court for the Northern District of California refused to compel arbitration on the ground that the policy of protecting investors prevailed over the policy of favoring arbitration. Judge Weigel found a prohibition against predispute arbitration agreements that paralleled the prohibition against such agreements for securities accounts.⁷⁵

The deference shown by some courts to CFTC jurisdiction, however, has not been evident in other cases. In *Shearson Hayden Stone, Inc. v. Lumber Merchants, Inc.*,⁷⁶ Judge King of the United States District Court for the Southern District of Florida refused to stay litigation pending determination of the customer's reparations proceeding. The court based its decision on the lack of authority requiring courts to defer to the CFTC and on the fact that the issues involved in the liquidation of the account were well within the expertise of the court to resolve.

In *Arkoosh v. Dean Witter & Co., Inc.*,⁷⁷ a customer filed an action in court to litigate a dispute arising out of market positions that had been liquidated after the customer did not meet a margin call. The brokerage firm made a written demand for arbitration and brought a motion to stay the litigation.

The customer argued that if the CFTC Act of 1974 prohibited an exchange from utilizing involuntary arbitration procedures, a member of an exchange was under a like prohibition. The court rejected the customer's argument and stayed the litigation pending conclusion of the arbitration. Judge Robinson reasoned that the prohibition of the Act applied only to exchange arbitration procedures; nonexchange arbitration was not affected.⁷⁸

74. *Id.* ¶ 20,227 (N.D. Cal. 1976).

75. *Accord*, *Ables v. ContiCommodity Servs., Inc.*, [1975-77 Transfer Binder] COMM. FUT. L. REP. (CCH) ¶ 20,266 (D.C. Wash. 1976). *Contra*, *Ames v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, [1975-77 Transfer Binder] COMM. FUT. L. REP. (CCH) ¶ 20,283 (S.D.N.Y. 1977).

76. [1975-77 Transfer Binder] COMM. FUT. L. REP. (CCH) ¶ 21,588 (S.D. Fla. 1976).

77. 415 F. Supp. 535 (D.C. Neb. 1976).

78. *Id.* at 538.

In passing, Judge Robinson stated that in an action not arising out of a violation of the Commodity Exchange Act but rather out of a violation of common law, a litigant would have a right under the seventh amendment to a trial by jury. Because the reparations procedure under the CFTC Act of 1974 did not provide for a trial by jury, Judge Robinson concluded that the courts rather than the CFTC would have jurisdiction over common law claims.⁷⁹

The *Arkoosh* and *Lumber Merchants* decisions show how brokerage firms may be able to preclude customers from reparations proceedings. If a brokerage firm can convince a court that its claim against a customer is a common law claim as opposed to a violation of the Commodity Exchange Act, a court can either order that the claim be arbitrated or retain jurisdiction to decide the controversy itself. Although the judges in *Arkoosh* and *Lumber Merchants* did not go so far as to say that they would stay the CFTC from deciding a controversy involving a common law claim, such a position would be the logical result of their decisions. Otherwise, concurrent proceedings could come to conflicting decisions on the same dispute. When the court appeared unwilling to defer to the administrative tribunal, this potential conflict compelled the CFTC administrative law judge in *Lumber Merchants* to resolve an impasse by dismissing the reparations proceeding.⁸⁰

The *Arkoosh* and *Lumber Merchants* decisions are predicated on a clear dichotomy between disputes under the common law and those under the Commodity Exchange Act. But there is no such clear dichotomy: A controversy can involve both common law and Commodity Exchange Act claims. Brokerage firms typically contend that customers owe money on a deficit incurred on a customer's account.⁸¹ Such a debt can be pleaded as a breach of contract or as a common count. Customers typically contend that brokerage firms are liable for fraud under the Commodity Exchange Act or rules promulgated under the Act. Because both common law and statutory claims can be involved in a dispute, the decisions in *Arkoosh* and *Lumber Merchants* raise the spectre of concurrent and potentially conflicting proceedings.

79. *Id.* at 540. Cf. *Rosenthal & Co. v. Bagley*, [Current Binder] COMM. FUT. L. REP. (CCH) ¶ 20,506 (N.D. Ill. 1977) (CFTC argued that a broker gives up right to a jury trial by choosing to engage in a business activity subject to comprehensive regulatory scheme. Judge Flaum declined to decide issue because of review provided under the Act, 7 U.S.C. § 18g). See generally *Schneider, Commodities Law and Predispute Arbitration Clauses*, 6 HOFSTRA L. REV. 129 (1977).

80. *Lumber Merchants, Inc. v. Shearson Hayden Stone, Inc.*, [Current Binder] COMM. FUT. L. REP. (CCH) ¶ 20,408 (CFTC 1977).

81. See Comment, *Arbitration of Investor-Broker Disputes*, 65 CALIF. L. REV. 120, 142-43 (1977).

The sensible course would be for the courts to defer to the jurisdiction of the CFTC. Under its reparations procedure, the CFTC decides preliminarily whether a reparations complaint alleges a violation of the Commodity Exchange Act.⁸² If the CFTC decides that plaintiff has not alleged a wrong under the Commodity Exchange Act, a court can proceed. If the CFTC decides that plaintiff has alleged a violation of the Act, the courts should hold any litigation in abeyance until it is shown that any decision which a court could make would not conflict with any decision the CFTC could make.⁸³

Before the CFTC Act of 1974, the United States Supreme Court referred antitrust cases to the primary jurisdiction of the Commodity Exchange Authority based on a general policy of deferring to the expertise of regulatory agencies.⁸⁴ In creating the reparations procedure in 1974, Congress created a special tribunal to give effect to the rights of customers under the Commodity Exchange Act. This specific mandate is certainly a more compelling reason to defer to the jurisdiction of the CFTC than a general policy of deferring to the expertise of regulatory agencies. By not deferring to the jurisdiction of the CFTC, the courts can thwart the intent of Congress. The appellate courts should decide that the courts must defer to the primary jurisdiction of the CFTC.

CONCLUSION

Although Congress intended section 5a of the CFTC Act of 1974 to break the chains of arbitration agreements, the CFTC rule section 180.3 has strengthened those chains. It is now far more difficult for the customer to avoid the arbitration agreement he has signed. If a customer wants to avoid arbitration, he will be forced to choose reparation. In cases that do not involve flagrant fraud, reparation before the CFTC should be better for a customer than a remedy through the courts. However, in cases involving flagrant fraud, a customer may have grounds for punitive damages;⁸⁵ and

82. 17 C.F.R. § 12.22 (1978).

83. *Cf. Stockwell v. Reynolds & Co.*, 252 F. Supp. 215 (S.D.N.Y. 1965) (court ordered arbitration of common law claims but stayed arbitration of common law claims until nonarbitrable federal securities fraud claims were decided).

84. *Chicago Mercantile Exchange v. Deaktor*, 414 U.S. 113 (1973); *Ricci v. Chicago Mercantile Exchange*, 409 U.S. 289 (1973).

85. No reported cases include an award of punitive damages for fraud involving commodity futures transactions. However, the author has tried cases in which punitives were awarded for fraud and churning. *Previte v. Lincolnwood, Inc.*, No.

one administrative law judge has held that a customer cannot obtain punitive damages in a reparations proceeding.⁸⁶ Although conceivably a customer could bring an action for exemplary damages in court concurrently with a reparations proceeding, the legal⁸⁷ and practical impediments to dual proceedings would be formidable. Therefore, one effect of the section 180.3 caveat will be to insulate brokerage firms from exemplary damages.

Another effect of section 180.3 has serious implications for the future. If the CFTC can so facily circumvent the intent of Congress by the section 180.3 caveat, no reason exists why the CFTC cannot use the same ploy to allow brokers to bind customers to arbitration to the exclusion of reparation. No statutory protection prevents waiver of the right to reparation. The protection of a customer's access to reparation is only through CFTC regulation.⁸⁸

Because customers should prefer reparation to arbitration, one can anticipate that many actions that otherwise would be filed in court will be filed as reparations. As the CFTC case load increases, the pressure to relieve the burden of a heavy case load will increase. Should the CFTC decide that reparations have become too burdensome, it could relieve itself of this burden by providing customers with a "voluntary" choice between arbitration and reparation. One can be certain that brokers will be lobbying for a regulation that will enable a customer to waive his right to reparation. Perhaps it is too soon for the CFTC to consider allowing customers to choose arbitration to the exclusion of reparation, but in time?⁸⁹ The life cycle of administrative agencies in

261861 (Super. Ct. of Santa Clara County, Cal. 1971) (actual damages of \$65,058 and punitives of \$50,000) (reported on other issues at 48 Cal. App. 3d 976, 122 Cal. Rptr. 194 (1975)); *Conley v. Peavey Co. Commodity Servs.*, No. C-31189 (Dist. Ct. of Sedgewick County, Kan. 1974) (actual damages of \$31,000 and punitives of \$70,000).

86. *Barker v. Commodity Management Syss., Inc.*, [Current Binder] COMM. FUT. L. REP. (CCH) ¶ 20,432 (CFTC 1977).

87. Under Reg. § 12.21 (7), a petition for reparation must allege "that no arbitration proceeding or civil court litigation, based on the same facts set forth and against the same parties named as respondents in the complaint, has been instituted or is presently pending." 17 C.F.R. § 12.21 (7) (1978).

88. *Romnes v. Bache & Co.*, [Current Binder] COMM. FUT. L. REP. (CCH) ¶ 20,535 (W.D. Wisc. 1977).

89. The pressure is already building. In February 1978 the Whitten Report discussed the case load of reparations proceedings:

The Chief Administrative Law Judge advised the Investigative Staff that he estimated that each judge can handle 25 reparations cases per year, giving his office a total capability of 100 such cases per year based on the present staff of 4 judges

The Chief Administrative Law Judge subsequently revised his estimate from 25 to 50 reparations cases which each judge can handle per year. Thus, the backlog of 285 reparations cases as of September 30, 1977, would represent a workload of either 2.85 or 1.43 years depending on which esti-

Washington begins with the vigor of youth but fades away into regulatory senility.⁹⁰ A young and virile CFTC may have already established the precedent for an old and tired CFTC to destroy its reparation jurisdiction.

mate is accurate. . . . The Chief Administrative Law Judge advised the Investigative Staff that a fifth judge has been included in the fiscal year 1979 budget. This would give a maximum capability of 250 reparations cases per year based on the more optimistic estimate. Thus even with an additional Administrative Law Judge, the backlog . . . can be expected to grow.

See SUBCOMM. ON AGRICULTURE AND RELATED AGENCIES APPROPRIATIONS OF THE HOUSE COMM. ON APPROPRIATIONS, 95TH CONG., 2D SESS., INVESTIGATIVE STUDY ON THE COMMODITY FUTURES TRADING COMMISSION 112 (Comm. Print 1978).

The CFTC expects to receive 1000 reparations complaints in 1978. See SENATE COMM. ON AGRICULTURE, NUTRITION, AND FORESTRY, 95TH CONG., 2D SESS., REAUTHORIZATION OF THE COMMODITY FUTURES TRADING COMMISSION 16 (1978).

90. See M. BERNSTEIN, *REGULATING BUSINESS BY INDEPENDENT COMMISSIONS* 74-95 (1966).

